Surface Transportation Board
RETAC Meeting October 4, 2018
Washington, DC

Meeting commenced at 0900 with opening remarks by Chairman Ann Begeman and Vice Chairman Deb Miller. Chairman Begeman indicated that a downsizing of the STB offices were underway and three more STB nominees are still pending in the Senate.

In attendance at the meeting were:

George Duggan, BNSF-Co-Chair	Brian Fuller, Southern Co.-Co-Chair	
Dan Sabin, IANR- Secretary	Mike Higgins, STB	Kristen Nunnally-STB
Ginger Adamiak, KCS	Kent Avery, PBF Energy	Bruce Blanton, USDA
Sean Craig, Dairyland Power	Jeff Eliason, CHS	Steve Ewers, NS
Jill Harrison, Contura Energy	Brad Hildebrand, Cargill	Robert Hulick, Trinity Rail
Greg Hynes, SMART	Mark Huston, Louis Dreyfus	Lee Johnson, Hess Corp.
Ed McKechnie, WATCO	Doug Noem, NCGA	Phillip Obie II Santee Cooper
James Rader, Greenbrier	Tony Reck, P&L	Jacqueline White-UP
Betty Whalen, Lower Colo River Authority		Shon Yates, CSX

RETAC Chairman George Duggan initiated introductions welcoming new members Jacqueline White from UP, Bette Whalen from Lower Colorado River Authority, Phillip Obie from Santee Cooper, Shon Yates from CSX and invited guest Kenny Rocker from UP.

RETAC Secretary Dan Sabin reported $962 remaining in the treasury before today's lunch payment.

Kenny Rocker, Executive Vice President Marketing and Sales was invited by Chairman Begeman to outline UP's recently announced Precision Railroading initiative highlighting that UP's velocity and inventory has not been meeting expectations, primarily due to network congestion; unforeseen service interruptions and subsequent lack of resources. These impacted service levels to the Network and is a main driver for changes.

UP's 2020 plan objectives are to improve safety, reliability and efficiency, moving from a focus of movement of trains to the direct focus on the movement of cars, blending of service networks and balancing resources. The plan is being developed with and by those closest to the work. This will also mean proactive communication with customers.

Mr. Rocker continued to discuss what can be expected from this:

- Focus on moving cars, not just moving trains
- Minimize car dwell time
- More reliable and predictable service
- Improve availability of locomotives and crews
- Create the potential for improved customer asset utilization

- Direct communication in advance of changes
- Technology with customers to express their requirements on service products
- Data shared with customers when lanes are impacted by 24 hours or less, notifying customers of service impacts
- New plan enables reliability improvement.

Initial new approaches will be implemented on UP's Northern Region and the North-South Corridors from Minnesota-Wisconsin-Illinois to the Gulf and West Texas.

Brad Hildebrand and Kent Avery asked about the operating ratio comments included in the initial public announcement and if this meant "Less with Less". Mr. Rocker replied that the gains in efficiency will result in a reduced operating ratio, and UP was developing a measurement that shows results vs. promised service levels, which improves reliability. Mark Huston asked how long the North-South corridor implementation will take to which Mr. Rocker responded that the shipment trackers would be available by the end of the year. Chairman Begeman's takeaway from the discussion regarding improving customer communication was essential to eliminate the customers inability to know who to call at UP. Mr. Rocker explained that UP will stay close to customers when changes occur. Lee Johnson reminded that the UP takeover of SP was awful and he hoped there would not be a similar occurrence with these changes.

STB requested continued communication from UP to maintain STB's monitoring of UP Progress and potential service issues during implementation.

Ed McKechnie provided the <u>Railroad Industry Report</u>, highlighting:

- Sharp decline in rail coal carloads with 2017 volumes of 3.24 million, 42% lower than in the peak year of 2008, equal to more than 27,000 120-car coal trains.

  Vice Chair Miller asked if thermal coal will go away completely or level off? Brian Fuller responded that volumes would slightly reduce over time. Phillip Obie explained that utilities have burned through large stockpiles so there may be a need to take on more coal now.

- Crude oil volumes terminated of only 128,000 carloads in 2017, down about 360,000 carloads from the peak year of 2014, up slightly in 2018.

  Kent Avery asked why the Canadian Railroads were not part of the RETAC group?

- Sand volumes up to 180,000 carloads in 2017 from 65,000 carloads in 2016 and continue to rise in 2018 to an estimated 190,000 carloads.
  Discussion about "resanding" with more sand used per existing well and most growth in the Permean Basin area in Texas.

- With coal down, railroads experiencing excess coal field capacity, but with crude and sand volumes, experiencing capacity issues, particularly in Wisconsin and West Texas.

- Ethanol 2016 volumes exceeded 360,000 carloads up slightly from 2015 and a new record, Ethanol has been stable and consistent.

- The railroads are reporting continued high levels of spending on Infrastructure and Equipment expected to be $24.8 billion in 2017 and includes over $12+ billion in capital for infrastructure and equipment and $12 billion for maintenance capital expenses. 2017 capital spending is down from the $30.3 billion in 2015.

- McKechnie continued with slides showing average train speeds and average terminal dwell time, noting that traditional performance decreases post December holidays and first quarter winter months, then returns to more normal performance.

  Steve Ewers (NS) reported that NS improved by 14% in September vs. May by hiring 1800 more train crew employees and leasing more locomotives. NS was trying to determine what traffic volumes will be expected in 2019.

  Ginger Adamiak (KCS) reported that KCS was experiencing congestion in their Southwest Division and south of the Mexican border crossing at Laredo, and has lowered their performance, but it should be resolved by the end of this year. Brad Hildebrand (Cargill) indicated that the Laredo embargo was hurting the grain industry business with Mexico.

  Shon Yates (CSX) indicated that CSX was making good improvement with locomotive availability on target and rehiring first level transportation supervisors (trainmasters). CSX does not report average train speeds. Export coal is growing.

  Jacqueline White (UP) said that UP was continually hiring more train crews.

  George Duggan (BNSF) reported that BNSF had slower train speeds and all locomotives were out of storage; crews are being hired with incentives; there have been shifts in various markets with PNW (Pacific North West) heavy and experiencing border issues. Coal has seen wet mine conditions slowing coal train turns. Capital spending since 2008 was based on an expected doubling of PRB (Powder River Basin) coal demand, which is not happening.

  Brad Hildebrand asked if the railroads would add "total employment" to the report.

Brian Feller (Southern Company) provided the <u>Utilities Industry Report</u>:

- Majority of coal-fired generation is 49% Midwest; 17% South; 17% West 17% Southeast and 0% Northwest.
- Utilities reported to the National Coal Transportation Association (NCTA) that 78% of them burn less than 10 million tons of coal; 11% burn 10-20 million tons; 6% burn 20-30 million tons and 6% burn 30-40 million tons. Respondents represent about 20% of the US coal burn.
- 56% of the NCTA respondents have rail sets of coal cars stored.
- Majority of NCTA respondents reported current coal inventory below 2017.
- Current coal inventory (average days of burn on hand for generators that run all year):
  Greater than 70 days – 11%; 50-70 days - 32%; 30-50 days - 50%; less than 30 days – 7%.
- Year over year actual coal-fired generation is:
  39% above prior year; 17% similar to prior year; 39% below prior year; 5% not reporting.

- Year over year actual rail deliveries are:
  11% above prior year; 28% similar to prior year, 56% below prior year; 5% not reporting.
- Rail cycle times are:
  6% faster than prior year; 44% similar to prior year; 44% slower than prior year; 6% not reporting.
- Rate recent service experience on NS:
  77% not applicable; 11% unsatisfactory; 6% average; 6% above average.
- Rate recent service experience on BNSF:
  28% not applicable; 17% unacceptable; 27% average; 28% above average.
- Rate recent service experience on UP:
  49% not applicable; 6% excellent; 11% unsatisfactory; 17% average; 17% above average.
- Rate recent service experience on CN:
  82% not applicable; 6% above average; 12% average.
- Rate recent service experience on CSX:
  83% not applicable; 17% average.
- No respondents served by KCS.

Lee Johnson provided the <u>Oil Industry Segment Update</u>:

- <u>Global crude oil demand</u> is growing and currently outpacing production, however,
  <u>***Surplus inventory expected in Q-2 2019.***</u>
- <u>WTI Spot Price</u> remains flat but volatile within a relatively narrow range.
- <u>US crude oil production</u> and exports trending upward; imports flat.
  50% of import from Canada.
- <u>US land rig count</u> is trending upward:
  August 2016 362 with 50% Texas;
  August 2017 672 with 59% Texas;
  August 2018 1,034 with 51% Texas.
- <u>Much US onshore growth remains in pipe centric Texas</u>
  Permian pipeline and refining capacity/production gap is narrowing.
- <u>Crude by Rail (CBR) volumes</u> have declined on an annual basis from 2014 to 2017, but increasing in 2018:
  2014 493,000 carloads
  2015 410,000 carloads
  2016 212,000 carloads
  2017 134,000 carloads
  2018 (First Half) 75,000 carloads, annualized to 150,000 carloads
- <u>Texas frac sand capacity development</u> (Texas Brown sand) has eliminated the Permian Basin shortage and has replaced some of the Northern White. Northern White sand is harder with higher crush capacity. Texas Brown is mostly truck moves. Most Northern White shipped to Bakken.
- <u>US production trending upward</u> now exceeding 10.7 MBD (Million Barrels Per Day)
- <u>Permian production trending upward</u> now exceeding 3.4 MBD.

- No apparent growth in Permian CBR through June, 2018. August 2018 production exceeded pipeline and local refining capacity. May see increased CBR market share, particularly to the west.
- Potential barriers to CBR:
  - Cost differential
  - Increased pipeline capacity
  -Limited rail loading terminal capacity
  -Availability of rail unloading capacity depends on market destination
  -Availability of new DOT 117 tank cars
- Bakken production trending upward now exceeding 1.2MBD
- Williston Basin Crude Oil Rail Modal Share was 59% in June 2014; 47% in June 2015; 29% in June 2016; 7% in 2017 and 19% in 2018 (June daily production).

Avg. Production Barrels Per Day		Rail Production Est. (barrels)
6/2014	1,092,519	644,586
6/2015	1,211,328	569,324
6/2016	1,027,131	297,868
6/2017	1,032,873	72,301
6/2018	1,225,510	232,847

CBR Destinations, February 2018:	
West Coast	60.2%
East Coast	37.5%
Gulf Coast	2.3%

- CBR trains per day from Bakken: 2014-10 trains/day; 2017 1 train/day; 2018 3-4 trains/day.

Kent Avery noted that Canadian crude is currently trading at a discount of $30 bbl because of the lack of pipelines from Alberta, now running 4-7 trains per day.

James Rader (Greenbriar) and Bob Hulick (Trinity) gave the rail car industry report:

- Though not near levels of 2014/2015 peaks, orders and backlogs of freight cars increased in Q-2 2018.
- Returning railcar demand in the energy and downstream energy markets should improve deliveries.
- After bottoming out at 45,000 deliveries in 2017, improving covered hopper and tank car demand is expected to drive growth over the next few years.
- Covered hopper deliveries are expected to grow due to near-term demand for >5,500 c.f. cars and improving demand for 3,500 – 5,500 c.f. in the longer term.
- Tank car delivery is expected to be strong by historical standards, but well off the production pace during the shale boom.
- As of Q-2 2018 there were 24,154 tank cars in the industry backlog, likely driven by higher tank car replacement demand and economic improvement.

COAL

- **Coal carloads** starting new normal after 2016 lull.
- **While improving from 2016,** coal carloads remained depressed with low natural gas prices, coal plant closures, and environmental regulations all acting as headwinds.
- **17.5% of open** coal hoppers and gondolas are currently in storage empty.
- **EIA forecasts coal production** to decline by 1% to 768 million short tons in 2018, despite a 10% increase in coal exports.

BIOFUELS

- **Ethanol by rail has moderated since Q-1 2017 peak**
- **USDA forecasts a nominal increase** in U.S. fuel ethanol production in 2018.
- **Tariffs and trade restrictions from China and Brazil** could also weigh on biofuel demand.
- **Of the 32,860 railcars that moved ethanol in Q-1 2018,** 56.9% were DOT 111s, 9.2% were CPC-1232s, and 33.3% were built to the DOT-117 standard.
- **Other biomass-based diesel products** are expected to grow 11% in the 2018-2019 season.

CRUDE OIL

- **U.S. CBR is expected to remain down while Canadian CBR expands**
- **Crude oil exports** (allowed as of December 2015) created more incentive for pipeline utilization to the Gulf Coast.
- **Due lack of new pipeline capacity,** Canadian crude oil carloads are expected to improve significantly over the next 2-3 years.
- **Railcars used to transport crude oil** has dropped by over 35,000 from the 2014 peak.
- **62.6% of all railcars used to transport crude oil in Q-1 2018** were CPC-1232s while 32% were DOT-117s.

PETROLEUM PRODUCTS

- **Mexico's energy liberalization is likely to drive carloads of petroleum products in 2018.**
- **U.S. carloads of petroleum products** excluding crude have rebounded, but remain 16% below peak levels last seen in Q-4 2014.
- **Domestic fuel consumption** is not expected to drive growth in the U.S.
- **Energy liberalization in Mexico** is expected to provide opportunity for U.S. fuels, but there is some uncertainty due to recent election results in Mexico.

NGLs

- **North America remains an advantaged geography for chemical production.**
- **North American polypropylene projects** are planned between 2020 and 2022 to exploit the continent's low cost inputs and high margins.
- **Export Opportunities and the petrochemical capacity** build out underway will drive up demand for natural gas liquids (i.e. propane and butane).

FRAC SAND

- **Frac sand by rail continues to grow but faces challenges from in-basin brown sand.**
- **Industrial sand deliveries** hit the bottom in Q-1 2016 but are up 43% since then.
- **In-basin Permian sand** is expected to impact sand car loadings in 2H 2018, some suppliers are opening mines in West Texas this year.
- **As of Q-2 2018** there were 11,912 small cube covered hoppers in the industry backlog.

DOT 117J and 120J200 Fleet Growth

- Fleet size has grown from zero in August 2014 to 19,486 cars with a 3% increase of 562 cars in July.

DOT 117R Fleet Growth

- Fleet size has grown from zero in January 2016 to 13,863 cars with a 10.2% increase of 1,272 cars in July.

Number of cars that need to be replaced/retrofitted to DOT-111J or DOT 117R by Service Date:

Crude Oil – 9,776 by May 1, 2025

Ethanol – 21,728 by May 1, 2025

Other Flammable Liquids – 25,892 by May 1, 2029

Total All tank cars – 57,396

Jeff Eliason (CHS) provided the Renewable Fuels Marketing Report

<u>U.S. Corn Situation</u>

	2016	**2017**	**2018**
Planted (Million Acres)	**94.0**	**90.2**	**89.1**
Harvested	**86.7**	**82.7**	**81.8**
Bushels Per Acre	**174.7**	**176.6**	**181.3**
Carry-In (Million Bushels)	**1,737**	**2,293**	**2,002**
Production	**15,148**	**14,604**	**14,827**
Imports	**57**	**40**	**50**
Total Supply	**16,942**	**16,937**	**16,879**
Feed Use-Residual	**5,472**	**5,450**	**5,575**
Food-Industrial	**6,884**	**7,060**	**7,130**
Exports	**2,293**	**2,425**	**2,400**
Total Use	**14,649**	**14,935**	**15,105**
Carry-out	**2,293**	**2,002**	**1,774**

- **<u>U.S. Fuel Ethanol September Production estimated at 15.911 annualized</u>**
- **<u>Production margins down from $0.38 per gallon Sept 1, 2010 to $0.24 per gallon Sept 1, 2018 with a high of $2.00 per gallon in 2013.</u>**
- **<u>In transit inventory increased with lower train speeds and increased dwell time. Seeing up to 13 days delay in Chicago interchange. This requires more tank cars into ethanol service with tank car lease prices climbing.</u>**
- **<u>Bio-Diesel production slightly over 100 million gallons in January 2016 to over 150 million gallons in June, 2018.</u>**
- **<u>Year round E-15 would help as would exports to China.</u>**
- **<u>Global demand for ethanol should exceed supply in 2019</u>**

<u>Jill Harrison (Contura Energy) provided the Coal Producer Update</u>

- **<u>Hurricane Florence effected coal loading at both Dominion Terminal and Norfolk Southern's Pier VI, increasing vessels at anchor. Other issues effect transportation schedules:</u>**

- **<u>Dominion Terminal unloads coal cars and stockpiles the coal, which generally adds moisture to the stockpile.</u>**

- **Pier VI unloads directly from the rail cars to ships, which often results in coal frozen in the cars.**
- **Global Coal Demand is expected to remain fairly stable through 2022, but is affected by pricing, tariffs and other unknowns.**
- **Australian coal is considerably more expensive than U.S. produced coal currently 17%, but has been as high as 43% in the past year.**
- **Steel Import Tariffs impact coal exports. In some cases countries are still selling cheaper steel to the U.S. markets, despite the steel tariffs.**
- **Example Harley Davidson's price of their motorcycles are up $2,200 since the steel tariffs have gone into effect.**
- **Turkey is implementing a 13% import tariff on met coal.**
- **Met coal, used in steel production is generally under 1 year contracts.**
- **Thermal coal, used for energy is generally under 3 month contracts.**

George Duggan (BNSF) provided a prepared statement for the Rail Industry Report:

(Copy below)

This portion of the meeting was completed at 1157 am.

Other agenda items:

Summary of Written Public Comments (if any)

Kristen Nunnally reported none received.

Roundtable Discussion – None

Discussion of possible dates for next meeting- STB will check calendars and advise.

Brad Hildebrand requested consideration for a virtual meeting/conference call instead of in person.

Meeting ended 1205pm. Lunch provided for RETAC members on 12th Floor.

Daniel R. Sabin (IANR), Secretary

Rail Industry Statement for the October 4, 2018 RETAC Meeting

Chairman Begeman, Vice Chairman Miller and fellow members of RETAC, good morning.

I am pleased to report that the U.S. economy has been improving since the 2016 slow down. Freight railroads operating in the United States continue to move an increasing amount of many of the things that drive the economy, connecting businesses with each other across the continent and with markets overseas over a rail network spanning close to 140,000 miles. I am also happy to report that freight railroads continue to do so safely due to a strong safety culture, employee commitment to safety, and massive investments in capital expenditures, maintenance, and new safety -enhancing technologies.

One of those new technologies is positive train control. By December 31, 2018, all Class I railroads will have completed PTC hardware installation, trained all relevant employees, and secured all needed radio bandwidth. Further, by the end of this year, PTC will be in operation on the vast majority — approximately 80 percent — of Class I PTC route-miles network wide, with some Class I railroads planning to be fully operational on their networks. Between 2018 and 2020, all Class I railroads will be completing PTC implementation, consistent with the statute. All railroads will continue their work on resolving technical operational challenges that will inevitably rise, which Congress anticipated and specifically provided flexibility for in its 2015 law. They also will be addressing the biggest remaining step in PTC implementation: interoperability with each other and with their tenant passenger and short line railroads.

As far as rail traffic is concerned August 2018, the most recent data available, was a strong month for rail traffic representing the sixth straight year-over-year monthly increase for total carloads. U.S. railroads originated 1.39 million carloads in August 2018, up 3.8% over August 2017. That's the biggest year-over-year percentage gain for total carloads in 14 months. Average weekly carloads in August 2018 were 277,205, the most for any month since October 2015, and 16 of the 20 carload commodities saw gains–the most since January 2015. Year-to-date carloads through August were up 1.9% over last year and up 6.5% over 2016. Commodities with the biggest year-to-date carload gains this year over last year include crushed stone, sand, and gravel, up 55,262 carloads; chemicals, up 48,715 carloads; and petroleum products, up 39,548 carloads. U.S. railroads also originated 1.44 million intermodal containers and trailers in August 2018, up 5.1%, over August 2017. 2018 will be another annual record for intermodal; through the first eight months of the year, intermodal volume is up 6.0%, or nearly 548,000 units.

As we have pointed out previously, railroads are a derived demand industry, meaning that the demand for rail traffic is a function of demand further down the economic chain for products that railroads haul. For some commodities, such as coal and grain, the level of rail traffic tends to rise or fall for reasons that have little to do with the state of the overall economy. Most rail categories, though, are sensitive to what's happening in the larger economy. The good news is the economic recovery though nine years old is still going strong. Still a concern, however, are trade policy discussions that add a level of uncertainty to future economic growth. Policymakers must be careful not to enact measures that could potentially harm this positive trend.

I would be remiss to not mention that we are looking forward to working with a full Surface Transportation Board after the Senate to acts on the nominations of Patrick Fuchs, Michelle Schultz, and Martin Oberman to be members.

Finally, all of us know Hurricane Florence brought much hardship to so many people in the southeast. Railroads continually strive to improve and implement effective strategies to protect employees, ensure network safety and mitigate impacts on their customers. Railroad personnel have worked extremely hard in very difficult conditions to repair washouts, clear debris from their tracks, and otherwise restore service to their customers as quickly and safely as possible. They deserve the highest praise for their efforts.

This concludes my comments on behalf of the rail sector. I would now invite the individual railroads to offer any observations they may have about their respective elements of the energy supply chain.